

# Paying Attention to Banks: Evidence from Offshore Deposits

Matthieu Chavaz (Bank of England)  
Pablo Slutzky (University of Maryland)

The views and opinions expressed in this article are those of the authors and do not necessarily reflect the views of the Bank of England

# Research Questions

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2. Do depositors discipline banks?
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Assumptions	What we do
Insured depositors never monitor, uninsured always do	Time varying attention
Frictionless deposit insurance	Frictions (payout lag)
Deposit insurance coverage is understood	Limited awareness

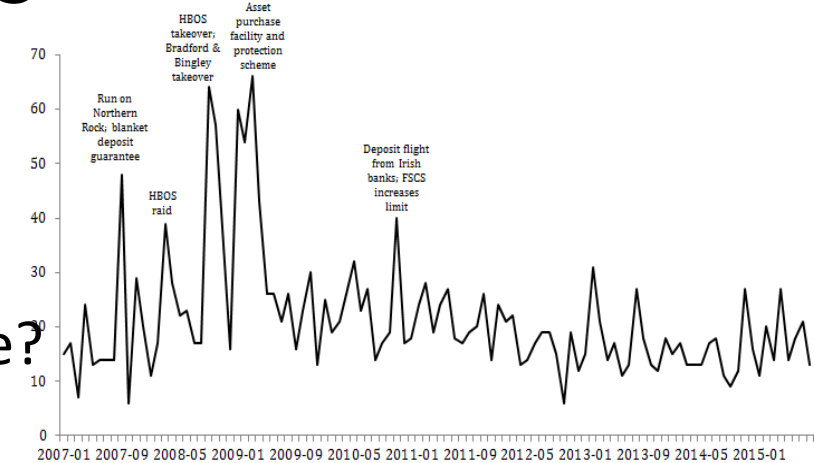
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## Claims against deposit takers

The FSCS will aim to pay compensation in the majority of cases within seven days of a bank, building society or credit union failing. Any remaining claims, which are likely to be more complex, will be paid within 20 working days.

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## 7.4. What did FSCS achieve in terms of raising awareness in 2016/17?

Consumer awareness of deposit protection is currently at 77% (up from <10% when the programme began). Depositors confidence that "my money is safe" is 78%, with a similar number saying the FSCS campaign makes them feel protected. 78% are reassured knowing FSCS exists and 63% say they trust banks and building societies more knowing FSCS protects them.

FSCS featured in almost 5,000 media articles and about 11,000 social media mentions during the year. Our PR messages reached 85% of all UK adults an average of 105 times during the year according to independent evaluation. The top messages were: there are limits to the protection FSCS provides; the range of FSCS protection; FSCS being funded by the industry.

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  - How to measure attention?
    - Use Google Search volumes (Da et al JF 2011)
  - How to assess the role of deposit insurance?
    - Exploit a peculiarity of the UK banking system

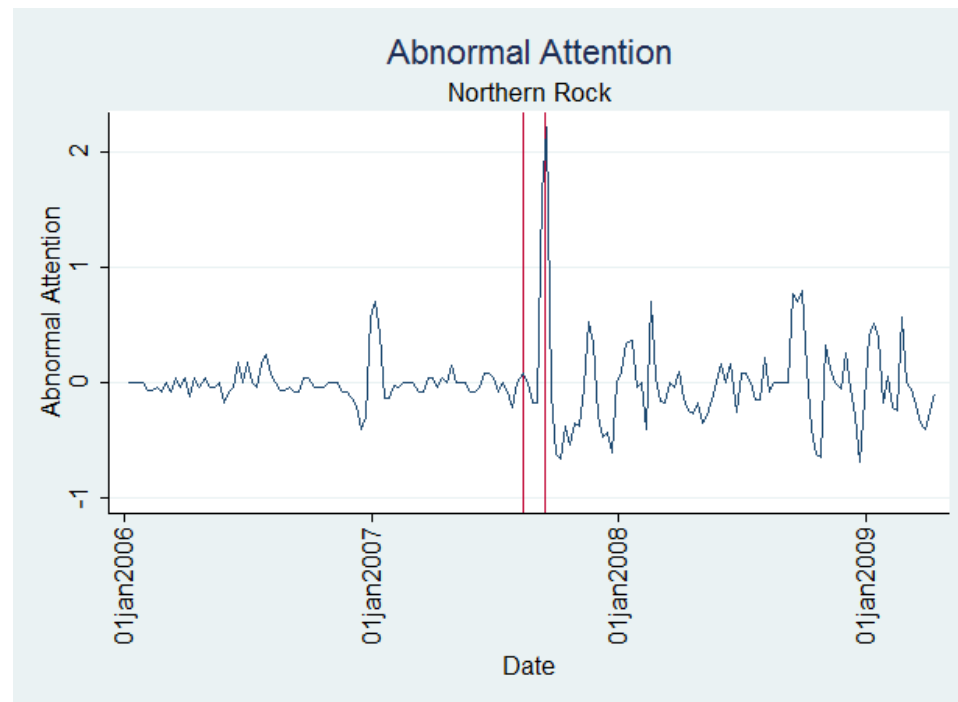
# Roadmap

1. Attention and market discipline
  - a) Deposit flows
  - b) Deposit rates
2. Deposit insurance, attention, and market discipline

# Attention and market discipline

- Search volume for each bank name by UK individuals (Barclays, Lloyds, etc.)

$$AbnAttention_{i,t} = \log(Frequency_{i,t}) - \log(MedianFrequency_{i,t-1;t-4})$$





# MARKET DISCIPLINE: DEPOSIT FLOWS

# Market Discipline: Deposit Flows

$$\Delta Deposits_{i,t} = \beta_1 Attention_{i,t-1} + \beta_2 Risk_{i,t-1} + \beta_3 Attention_{i,t-1} \times Risk_{i,t-1} + Bank_i + Month_t + \varepsilon_{i,t}$$

## 1. Funding liquidity risk

- *Stable funding = Individual Deposits/Total Liabilities*
  - Best predictor of failure (Mio, 2015)

## 2. Solvency risk

- *Capitalisation = Tier 1 Capital/Total Liabilities*

# Market Discipline: Deposit Flows

<i>Depositor Type:</i>	Individuals	Government	Public Firms	Financial Firms	Private Firms	All
Stable Funding	-0.04 (0.05)	-0.25 (0.19)	-0.22 (0.97)	-0.06 (0.24)	-0.24* (0.14)	-0.08 (0.07)
Attention	-0.09** (0.04)	0.06 (0.16)	-0.16 (0.78)	-0.23 (0.20)	-0.07 (0.12)	-0.14** (0.07)
Attention x Stable Funding	0.15** (0.07)	0.05 (0.26)	0.29 (1.32)	0.21 (0.32)	0.12 (0.19)	0.21** (0.10)
Bank fixed effects	Yes	Yes	Yes	Yes	Yes	Yes
Month fixed effects	Yes	Yes	Yes	Yes	Yes	Yes
Observations	951	891	398	935	908	951

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This effect is driven by retail depositors only



# MARKET DISCIPLINE: DEPOSIT RATES

# Market Discipline: Deposit Rates

- Deposit rates data from all UK banks (240)
- Daily frequency
- Detailed product characteristics (41,000 deposit products)
  - Classify deposits into ~400 unique product categories


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<input type="checkbox"/> <b>Britannia</b>	1.10%	Instant	£500	Online ✓ Branch ✓ Postal ✗ Phone ✓	<a href="#">Details...</a>	
<input type="checkbox"/> <b>Leeds Building Society</b>	1.05%	31.05.18	£1000	Online ✓ Branch ✗ Postal ✗ Phone ✗	<a href="#">Details...</a>	
<input type="checkbox"/> <b>Charter Savings Bank</b>	1.01%	None	£1000	Online ✓ Branch ✗ Postal ✗ Phone ✗	<a href="#">Details...</a>	
<input type="checkbox"/> <b>Ford Money</b>	1.00%	None	£1	Online ✓ Branch ✗ Postal ✗ Phone ✓	<a href="#">Details...</a>	

# Market Discipline: Deposit Rates

$$Rate_{p,i,j,t} = \beta_1 \sum_{l=1}^4 Attention_{i,t} + \beta_2 Risk_{i,t-1} + \beta_3 \sum_{l=1}^4 Attention_{i,t} \times Risk_{i,t-1} + \gamma_{i,j} + \theta_{p,t} + \varepsilon_{p,i,j,t}$$

- $\gamma_{i,j}$  Bank-jurisdiction fixed effects
- $\theta_{p,t}$  Product-time fixed effects

# Market Discipline: Deposit Rates

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<i>Dependent variable:</i>	<i>Deposit Rate<sub>i,p,j,t</sub></i>			
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Stable Funding	-0.76 (0.49)	-0.46 (0.46)	-0.46 (0.46)	
CDS				-0.03 (0.03)
<b>Attention</b>	0.27*** (0.09)		0.35*** (0.11)	0.05*** (0.02)
Attention x Stable Funding	-0.25*** (0.08)		-0.31*** (0.10)	
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News x Stable Funding		-0.00 (0.17)	0.08 (0.20)	
News x Capital		0.67 (0.94)	1.50 (1.25)	
Product-month FE	Yes	Yes	Yes	Yes
Bank-jurisdiction FE	Yes	Yes	Yes	Yes
$R^2$	0.84	0.85	0.85	0.88
Observations	204,030	144,452	144,452	42,633

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Attention triggers market discipline

# Supply of Information

- UK newspapers coverage

$$\text{Article Negativity}_{a,i,t} = \frac{\#(\text{Negative Words})_{a,i,t} - \#(\text{Positive Words})_{a,i,t}}{\#(\text{Words})_{a,i,t}}$$

$$\text{Negative Coverage}_{i,t} = \text{Mean Article Negativity}_{i,t} * \#(\text{Articles})_{i,t}$$

- Financial markets: CDS spreads

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Supply of information does not affect market discipline  
Attention to banks does



# THE ROLE OF DEPOSIT INSURANCE

# Offshore centers

- Many UK banks offer same product in Crown dependencies
  - Isle of Man; Guernsey; Jersey
- Comparable environment
  - Currency; citizens; laws
  - Despite self-governing
- Onshore / offshore depositors face same bank risk
- But different deposit insurance



# Offshore depositors

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## The savers they forgot to mention

Spare a thought for those who, through no fault of their own, put their money in offshore banks and now find they're not covered by the rescue plan



# Offshore depositors

## The savers they forgot to mention

Spare a thought for those who, through no fault of their own, put their money in offshore banks and now find they're not covered by the rescue plan



- 85% of deposits in the Isle of Man held by retail customers
- 69% of depositors in the Isle of Man have balances under £20,000

# Offshore deposit insurance

- Pre-crisis: none
- Post-crisis: £50,000 per qualifying deposit
- But limited credibility:

*"...in the event of a very large covered bank failing, or in a systemic crisis, the Deposit Compensation Scheme is unlikely to be in a position to provide the full amount of compensation due to you in a timely manner."*

- £100 Million payout cap (~0.1% of total balances)
- ex-post funding

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Offshore

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Find no evidence of market discipline for liquidity risk

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Find no evidence of market discipline for liquidity risk  
Both onshore and offshore

# Deposit Insurance

	(1)	(2)
<i>Dependent Variable:</i>	<i>Deposit Rate<sub>i,p,t</sub></i>	
Capitalisation	2.64** (1.32)	2.63** (1.32)
Stable Funding	-0.76 (0.51)	-0.76 (0.51)
Offshore x Stable Funding	-1.85 (1.45)	-1.81 (1.43)
Offshore x Capitalisation	-7.09*** (1.41)	-6.93*** (1.40)
Attention		0.25** (0.10)
Offshore x Attention		1.64*** (0.41)
Attention x Stable Funding		-0.23** (0.09)
Attention x Capitalisation		-0.73 (0.48)
Offshore x Attention x Stable Funding		-1.58*** (0.36)
Offshore x Attention x Capitalisation		-8.02*** (2.80)
Product-month FE	Yes	Yes
Bank-jurisdiction FE	Yes	Yes
$R^2$	0.84	0.84
Observations	203,021	203,021

Find no evidence of market discipline for liquidity risk

Both onshore and offshore

However, with attention, discipline for onshore accounts

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Find no evidence of market discipline for liquidity risk

Both onshore and offshore

However, with attention, discipline for onshore accounts

The effect is stronger for offshore accounts

# Sophistication

**Table 11** OFFSHORE VS. ONSHORE COMPARISON FOR DIFFERENT DEPOSIT SIZES

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
<i>Dependent variable=rate for minimum deposit amount:</i>	1k	5k	25k	50k	100k	125k	150k
Offshore x Attention x Capitalisation	1.34 (9.88)	3.69 (7.78)	-4.61* (2.65)	-3.89* (2.12)	-3.37* (1.96)	-3.30* (2.0)	-3.72* (2.14)
Offshore x Attention x Stable Funding	-0.66 (0.79)	-0.3 (0.4)	-1.09*** (0.34)	-1.36*** (0.37)	-1.32*** (0.38)	-1.29*** (0.4)	-1.27*** (0.4)
Product-month FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Bank-jurisdiction FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Observations	168916	195399	204745	194813	192300	190215	190215
$R^2$	0.835	0.843	0.839	0.837	0.843	0.845	0.845

# Sophistication

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# Summary

- First paper to incorporate attention to banks, intermittent monitoring
- Active attention is necessary for banks to be disciplined
  - Maybe why inconclusive results so far
- Discipline stronger with weak deposit insurance scheme
- Discipline even in the presence of an almost frictionless insurance scheme
  - Frictions
  - Disclosure
  - Attention



**THANK YOU**